

1 SHEPPARD, MULLIN, RICHTER & HAMPTON LLP
A Limited Liability Partnership
2 Including Professional Corporations
AARON J. MALO, Cal. Bar No. 179985
3 KYLE MATHEWS, Cal. Bar No. 218384
650 Town Center Drive, 4th Floor
4 Costa Mesa, California 92626
Telephone: 714.513.5100
5 Facsimile: 714.513.5130
E mail amalo@sheppardmullin.com
6 kmathews@sheppardmullin.com

7 Attorneys for BO1BO2 United Management,
LLC; Beach Orangethorpe, LLC; and
8 Beach Orangethorpe II, LLC

9
10 **UNITED STATES BANKRUPTCY COURT**
11 **CENTRAL DISTRICT OF CALIFORNIA**
12 **SANTA ANA DIVISION**

13
14 In re:
15 THE SOURCE HOTEL, LLC, a
California limited liability company,

16
17 Debtor and Debtor in
Possession.

Case No.: 8:21-bk-10525-ES
Chapter 11

18
19 **LENDERS' OBJECTION TO**
20 **ASSUMPTION AND ASSIGNMENT**
21 **OF EXECUTORY CONTRACT**

Hearing

Date: September 30, 2021
Time: 2:00 p.m.
Place: ZoomGov

22
23 The Source at Beach Secured Parties (defined below) do not object to the Debtor's
24 sale motion, nor do they object to the assignment and assumption of the Ground Lease.
25 Their only objection is directed to the Debtor's attempt to assign the Ground Lease without
26 curing defaults occurring thereunder.
27
28

1 Beach Orangethorpe, LLC, a California limited liability company ("BO1"), Beach
2 Orangethorpe II, LLC, a California limited liability company ("BO2"), and BO1BO2
3 United Management LLC, a California limited liability company (in its capacity as
4 collateral agent for the Source at Beach Lenders (as defined below), "Collateral Agent"
5 and collectively with BO1 and BO2, the "Source at Beach Secured Parties") hereby object
6 to the assumption and assignment of the below-described executory contract, as proposed
7 in the Debtors' *Motion for Entry of an Order: (1) Authorizing Sale of Substantially All of*
8 *the Debtors' Assets; (2) Authorizing the Debtor's Assumption and Assignment of Ground*
9 *Lease and Determining Cure Amount; (3) Waiving the 14-Day Stay Periods Set Forth in*
10 *Bankruptcy Rules 6004(h) and 6006(d); and (4) Granting Related Relief* [Docket No. 227]
11 (the "Sale Motion") filed on September 9, 2021 in the above-captioned case.¹ Pursuant to
12 the Sale Motion, the Debtor has proposed to assume and assign the Ground Lease by and
13 between The Source at Beach, LLC ("Project Owner") and the Debtor dated April 6, 2015
14 (attached hereto as Exhibit A) (the "Ground Lease") and has proposed a related \$0 cure
15 amount.

16 The BO1, BO2, Beach Orangethorpe Ventures, LLC, a California limited liability
17 company ("BO3") and Beach Orangethorpe Source, LLC, a California limited liability
18 company ("BO4") and together with BO1, BO2, BO3 and BO4, collectively, the "Source at
19 Beach Lenders") provided financing to Project Owner secured by certain deeds of trust
20 (collectively, the "Deeds of Trust").² The Deeds of Trust encumber the Project Owner's
21 fee interest in the entire "Source at Beach" project, including the Hotel Complex Premises
22 (as defined in the Ground Lease), as well as the adjacent mall and office park (the entire
23 project encumbered by the Deeds of Trust is referred to hereinafter as the "Source at Beach
24 Project"). The Source at Beach Lenders entered into a Ground Lessor's Consent, Estoppel

25 ¹ Counsel for Source at Beach Secured Parties brought this issue to the attention of Debtor's counsel on September 14, 2021 and
26 requested an extra two court days' extension within which to file this Objection. While the Debtor was willing to grant the
27 extension, Shady Bird Lending, LLC objected. This resulted in the need to file this Objection on September 15, 2021, to avoid the
28 need to file on Yom Kippur. We ask the Court's indulgence with any typos that may have resulted from this rushed filing.

² True and correct copies of the Deeds of Trust are attached hereto as Exhibits B-1, B-2, B-3 and B-4.

1 Certificate and Fee Mortgage Agreement, dated as of April 6, 2015, whereby the Source at
2 Beach Lenders subordinated their interests in the Hotel Complex Premises to the Ground
3 Lease on the terms and conditions set forth therein.

4 A recent preliminary title report (attached hereto as Exhibit C) reveals the presence
5 of over 40 mechanics liens and *lis pendens* on the Source at Beach Project arising from the
6 Debtor's failure to pay construction costs.³ Unfortunately, the mechanics lien claimants
7 did not limit their liens to the Debtor's leasehold interest in the Hotel Complex Premises.
8 Instead, many of the mechanics liens were filed against the Project Owner and purport to
9 encumber the Project Owner's fee interest in the Hotel Complex Premises and/or other
10 parts of the Source at Beach Project.

11 Pursuant to Article 12 of the Ground Lease, the Debtor agreed that "it will pay, or
12 cause to be paid, all costs of labor, services and/or materials supplied in the prosecution of
13 any work, done, or caused to be done, on the Hotel Complex Premises, and [Debtor] will
14 keep the Hotel Complex Premises free and clear of all mechanics' liens and other liens on
15 account of work done for [Debtor] or persons claiming under [Debtor]." The Debtor was in
16 default under the Ground Lease pre-petition, and remains so today. Allowing the
17 mechanics liens to persist on the Hotel Complex Premises and other parts of the Source at
18 Beach Project constitutes a default under the Ground Lease.

19 Section 365(b)(1) of the Bankruptcy Code provides that:

20 If there has been a default in an executory contract or
21 unexpired lease of the debtor, the trustee may not assume such
22 contract or lease unless, as the time of the assumption such
23 contract or lease, the trustee . . . (A) cures, or provides
24 adequate assurance that the trustee will promptly cure, such
25 default other than a default that is a breach of a provision
26 relating to the satisfaction of any provision...relating to a
27 default arising from any failure to perform nonmonetary
28 obligations under an unexpired lease of real property, if it is
impossible for the trustee to cure such default by performing

³ Due to the voluminous nature of the mechanics lien documentation, only the report has been attached to this Objection. Copies of the mechanics liens are available upon request.

1 nonmonetary acts at and after the time of assumption, except
2 that if such default arises from a failure to operate in
3 accordance with a nonresidential real property lease, then such
4 default shall be cured by performance at and after the time of
5 assumption in accordance with such lease...; (B) compensates,
6 or provides adequate assurance that the trustee will promptly
7 compensate, a party . . . for any actual pecuniary loss . . .
8 resulting from such default; and (C) provides adequate
9 assurance of future performance under such contract or lease.

10 11 U.S.C. § 365(b)(1).

11 Courts in this Circuit hold that “curing” defaults under an executory contract for
12 Section 365 purposes requires cures of both monetary and nonmonetary defaults. *See In re*
13 *Claremont Acquisition Corp., Inc.*, 113 F.3d 1029, 1033 (9th Cir. 1997) (In general, a
14 debtor must cure all defaults, both monetary and nonmonetary, prior to the assumption and
15 assignment of an executory contract.); *see also In re Arriva Pharmaceuticals, Inc.*, 456
16 B.R. 419, 423-24 (Bankr. N.D. Cal. 2011) (“The cure requirement applies to both
17 monetary and nonmonetary defaults”); *See In re 2712 Mission Partners, L.P.*, No. 08–
18 32226 TEC, 2010 WL 431738, *3 n.4 (Bankr. N.D. Cal. Jan. 25, 2010) (in parallel
19 analysis, finding that section 1142(2)(A) requires the cure of almost all non-monetary
20 defaults except those enumerated in 365(B)(2)(D)). In other words, in order to “cure” the
21 defaults under the Ground Lease for purposes of assumption and assignment, the Debtor
22 must do more than merely pay the \$0 “cure amount” referenced in the Sale Motion; it must
23 also cure the existing non-monetary defaults created by allowing mechanics liens to affix
24 to the Hotel Complex Premises and other parts of the Source at Beach Project. That can be
25 easily accomplished here if the Debtor pays amounts owed to the holders of the mechanics
26 liens.

27 While the Source at Beach Secured Parties do not specifically object to the \$0
28 monetary cure amount set forth in the Sale Motion, the Source at Beach Secured Parties
dispute that such a \$0 payment is all that is required to cure the defaults under the Ground
Lease. The Source at Beach Secured Parties ask that the Court require any assignee of the

1 Ground Lease fully cure all performance obligations under the Ground Lease as a
2 condition to any assumption and assignment, as required by Section 365(b)(1), including
3 the removal of all mechanics liens and *lis pendens* from the Source at Beach Project.
4 Without limiting the foregoing, any “cure” must include the requirement to remove any
5 mechanics liens and other liens on the property arising out of work done for the Debtor or
6 persons claiming under the Debtor.

7 The Source at Beach Secured Parties hereby expressly reserve all rights and
8 remedies they may have against the Debtor under the Ground Lease and Section 365 of the
9 Bankruptcy Code.

10 Dated: September 15, 2021

11 SHEPPARD, MULLIN, RICHTER & HAMPTON LLP

12 By



13 AARON J. MALO

14 KYLE J. MATHEWS

15 Attorneys for BO1BO2 United Management, LLC
16 Beach Orangethorpe, LLC
17 Beach Orangethorpe II, LLC
18
19
20
21
22
23
24
25
26
27
28